United States of America
IN THE

Supreme Court of the United States

OCTOBER TERM, 1944

No. 1323 94

LOUIS HAMBURGER and SAMUEL HAMBURGER,
Petitioners,
vs.
COMMISSIONER OF INTERNAL REVENUE,
Respondent

PETITION FOR WRIT OF CERTIORARI AND BRIEF IN SUPPORT THEREOF

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AUTHORITIES CITED

Statutes:

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LOUIS HAMBURGER and SAMUEL HAMBURGER,
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Respondent

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT

TO THE HONORABLE, THE CHIEF JUSTICE AND THE ASSOCIATE JUSTICES OF THE SUPREME COURT OF THE UNITED STATES:

Your Petitioners, Louis Hamburger and Samuel Hamburger, respectfully represent that:

SUMMARY STATEMENT OF THE MATTERS INVOLVED

This case involves a substantive question of income tax law, the application by the lower court of the doctrine of *Helvering v. Clifford,* 309 U. S. 331, holding that the income of a short term trust with a reversion to the grantor, who was himself trustee with elaborate powers, was taxable to the grantor under Section 22 (a) I. R. C. to the trusts in the instant case where none of the decisive elements of the Clifford case were present.

In the trusts at bar there was a complete transfer of title to the trustee who was not the settlor; the term was as long as the law permitted, to-wit, the survivor of two lives in being; there was no reversion whatsoever to the settlor; the trusts were irrevocable and unalterable; the settlor was expressly excluded from any benefit directly or indirectly in corpus or income; the trustee's powers of control were powers in trust and expressly stated to be exercisable only for the benefit of the trust; the settlor retained no substantial property so that it could not be said that the settlors did not feel the poorer after the transaction. The trusts provided for discretionary accumulation during the lifetime of the settlor but provided for minimum income and corpus distribution thereafter. The trusts also reserved to the settlor the power to change the beneficiaries (which power was never exercised) subject to the limitation of the instrument excluding the settlor from benefitting thereby directly or indirectly and the trusts were created by each petitioner naming his brother as trustee simultaneously with similar action by the other brother. It is apparently on the basis of these two last named factors that the Court below held the income taxable to the settlors.

The taxes involved in the years in question amount to over $73,000.00. If the decision below is applied to later years up to the present date, the deficiency would total approximately $500,000.00, a sum greatly in excess of the total income of the petitioners for the corresponding periods.

STATEMENT OF THE CASE

The facts are undisputed. The Petitioners are brothers, citizens of the United States and residents of Detroit, Michigan. They went into the waste material business together some 18 years ago, first as co-partners, then as equal shareholders of H. B. Hamburger nad Company, a Michigan corporation (R. 57). In December, 1937, the Petitioners created the trusts here involved (R. 57).

The trusts were for the benefit of their respective wives and children with a separate trust for the benefit of each beneficiary. Samuel created two trusts for his wife and one child and Louis created five trusts for his wife and four children (R. 58-62). Each transferred all of his capital stock in the corporation to the trusts equally divided among the trusts (R. 61). The stock constituted all of their property other than their homes which they owned jointly with their wives and about $45,000.00 of life insurance which was not paid-up and required the payment of premiums (R. 61). Each trust contained identical terms varying only in the name of the primary beneficiary (R. 105).

On November 3, 1938, another trust was created by Samuel for his child, Sola Jane, who was born after the original trusts were created (R. 57). This was pursuant to a provision common to all the trust agreements that any

after-born child should become a beneficiary on an equal basis (R. 110).

Each trust created by Samuel named Louis as trustee (R. 106) and each trust created by Louis named Samuel as trustee (R. 58, 59). The term of each trust is for the life of the survivor of Samuel Hamburger and Louis Hamburger. The income is to be paid to the named beneficiary or in the discretion of the trustee accumulated, but with minimum guaranteed distributions after Settlor's death. There is an express prohibition against payment for support. There is no reversion (R. 106-112). The discretion of the trustee has been exercised in favor of accumulation (R. 78).

Power is reserved to the settlor to change the beneficiary, add a beneficiary or increase or decrease the beneficiary's interest. The settlor is expressly forbidden to name himself or his estate as beneficiary (R. 111). This power is subject to the limitations contained in the trust agreement, among which is paragraph 10 which provides as follows:

> "That the said Settlor or his estate shall not directly or indirectly become vested or revested with any legal or beneficial interest in the trust property or its proceeds, either of income or principal, nor shall any income, principal, or interest, beneficial or legal, in the trust property be held or accumulated for future distribution to the Settlor or to his estate, nor shall the same be distributed to Settlor or to his estate, nor shall any part of the principal, income, or proceeds of the trust property, or any part thereof, ever be applied to the payment of premiums upon policies of insurance upon the life of the Settlor, nor be used or applied for the support of the Settlor or for the benefit of Settlor or his estate, nor used to satisfy any obligation of the Settlor or his estate" (R. 111).

And paragraph 14 which provides as follows:

> "This trust is hereby declared to be irrevocable and there shall be no power to terminate, alter, or amend this trust instrument, nor shall there be any power on the part of anyone to revest in the Settlor or his estate any part of the corpus of the trust" (R. 112).

Powers of investment not limited to legal trust investments and power of control and management were vested in the trustee but in trust and for the benefit of the trust "with a view to create the greatest income therefrom, and to increase the value of the trust property to the best of the Trustee's ability" (R. 108).

There is a spendthrift clause (R. 110) and also a provision that a minimum amount of not less than $50.00 per month nor less than 50% of the Trustee's compensation nor less than 50% of the net monthly income shall be paid to the beneficiary after the Settlor's death (R. 109). Upon termination of the trust, the property, principal, income and any accumulations is distributable to the then beneficiary (R. 112). The purpose of creating the trust was to accumulate money for the wife and children of the Settlor and protect the business in case of the death of either of them and to make provision for subsistence of the family of each Settlor after his death (R. 64, 67).

In December of 1938, the corporation was dissolved. From the formation of the trusts on December 27, 1937 until the dissolution of the corporation on December 30, 1938, Louis continued to be President of the corporation and Samuel continued to be Secretary-Treasurer and each received a salary, which before minor deductions, was $17,500.00 (R. 70-72).

Upon the liquidation of the corporation, all the property was conveyed to the trusts (R. 62) who elected to be taxed

upon the gain under Section 112 (b) 7 of the Revenue Act of 1938 (R. 17). This gain was in the amount of $103,-522.17 (R. 55) and was included in the return of the trusts which duly paid their tax thereon. Such gain is likewise included in the amount of income assessed against the petitioners herein (R. 97). On December 27, 1938, Samuel, individually and as trustee under the several trusts, and Louis, individually and as trustee under the several trusts, entered into a written partnership agreement effective after December 30, 1938 (R. 113-118). This agreement provided that the parties become and remain partners in the business of dealing with waste and steel products (R. 113). The capital was to consist of the assets received in the liquidation of the corporation (R. 113, 114). All of the capital was furnished by the trusts which had received all of the assets of the corporation (R. 114). The partnership was to be managed by Louis and Samuel Hamburger who were to receive 15% each of the net profits as compensation for their services (R. 115), the remaining 70% of the profits to be divided between the trusts in proportion to the interests transferred to the partnership (R. 115, 116). On liquidation, Samuel and Louis would receive no part of the capital of the partnership (R. 113-118).

This partnership has continued to operate the business since December, 1938 (R. 62). Samuel and Louis have each been receiving 15% of the net income (R. 62). They have no other income (R. 61). They have continued to conduct the business as managing partners (R. 70).

Petitioners have continued to support their wives and children from their portion of the net profits of the partnership (R. 78). The income of the trusts has been accumulated and invested in United States Government Bonds to the amount of $100,000.00 (R. 77). No change of beneficiaries has occurred (R. 63) other than the admission of

the after-born daughter of Samuel pursuant to the terms of paragraph 7 of the trust agreement (R. 57, 110).

The trusts have duly reported and paid tax upon dividends received from the corporation, the capital gain on liquidation and the 70% of the net earnings of the partnership. Petitioners have duly reported and paid tax on their salaries from the corporation and their portion of the net profits of the partnership.

One of the Petitioners at one time borrowed from \$15,000 to \$18,000 from the trusts (R. 63). There is no proof or claim that the other petitioner did so. The circumstances of this transaction will be discussed within.

The Commissioner issued his 90-day letter to each Petitioner May 25, 1942 for the years 1937-1940 inclusive asserting the deficiencies totaling \$36,626.15 (R. 15) in the case of Louis and \$37,615.78 (R. 36) in the case of Samuel. The Petitioners on August 21, 1942 filed their petitions for redetermination of the alleged deficiencies with the Tax Court of the United States (R. 5, 25). The cases were consolidated for hearing and decision and were tried before the Tax Court of the United States at a circuit hearing in Detroit, Michigan on September 28, 1943 and Judge Sternhagen presided (R. 3). His opinion and findings of fact were promulgated December 24, 1943 in the form of a memorandum opinion (R. 87-97) and hence not reported.

Petitioners' motion for review by the entire Tax Court was denied (R. 4). On February 14, 1944, a decision of the Tax Court was entered in favor of the Commissioner and against taxpayers, holding Louis Hamburger liable for deficiencies aggregating \$36,113.10 and Samuel Hamburger \$37,102.74 (R. 98, 99).

Taxpayers on May 1, 1944 filed their petition for review by the United States Circuit Court of Appeals for the Sixth Circuit (R. 99). By stipulation approved by the Circuit Court of Appeals the two cases were consolidated for hearing and decision under a single record (R. 105). The cause was argued and submitted on February 12, 1945 and judgment was entered March 12, 1945 affirming the decisions of the Tax Court on the grounds and for the reasons set forth in the opinion of the Tax Court. The order of the Circuit Court of Appeals is reported in 147 Fed. (2d) 856. No opinion was rendered by the Circuit Court of Appeals. The findings of fact and opinion of the Tax Court may be found on pages 87-97 of the record.

THIS PETITION PRESENTS THREE QUESTIONS

I.

After the creation of the trusts did the Petitioners retain such rights as to be still the owners of the property transferred within the meaning of Section 22 (a) of the Internal Revenue Code so that the income from such property remained taxable to the Petitioners?

The Tax Court and the Circuit Court of Appeals both determined that the Petitioners remained the owners of the trust property and were taxable on the income therefrom.

II.

Under Section 181-182 of the Internal Revenue Code, may Petitioners be taxed for the share of partnership income belonging to the other partners pursuant to a written partnership agreement?

The Tax Court and the Circuit Court of Appeals both held that the petitioners were taxable on all of the partnership income.

III.

Is ownership of trust property for tax purposes where the facts are undisputed and evidenced by written agreements a question of law within the scope of review by the Appellate Courts on appeal from the Tax Court?

The Circuit Court of Appeals held that it was not reviewable. The Tax Court, of course, did not pass upon this question.

BASIS OF JURISDICTION

Jurisdiction is invoked under 28 U. S. C. 347.

Petitioners are advised and believe that the judgment of the Circuit Court of Appeals is erroneous and contrary to the just rights of Petitioners, and that this Court should require said cause to be certified to this Court for its review and determination in conformity with the provisions of the Acts of Congress in such case made and provided.

REASONS FOR GRANTING PETITION

Certiorari should be granted for the following reasons:

1. The decision of the Circuit Court of Appeals is in conflict with a decision of another Circuit Court of Appeals on the same matter, *i.e.*, the decision of the 10th Circuit in the case of *Armstrong v. Commissioner*, 143 F (2d)

700 C.C.A. 10 and with the decision of the 1st Circuit in *Commissioner v. Branch,* 114 F (2d) 985 and with the decision of the 7th Circuit in *Commissioner v. Betts,* 123 F (2d) 534. In each of these cases, although the circumstances were more closely within the framework of *Helvering v. Clifford,* 309 U. S. 331 than in the case at bar, the several circuits held that the income from the trusts there involved was not taxable to the grantors whereas the 6th Circuit in the instant case held that it was.

2. The Court below has decided a federal question in a way probably in conflict with applicable decisions of this Court in that this Court in *Helvering v. Stuart,* 317 U. S. 154 decided that the power to change beneficiaries (to one other than the grantor) and the fact that the trusts involved were reciprocal did not require the taxation of the income therefrom to the grantors. The decision below taxes the income of the trust in this case to the grantors primarily because of the existence of these two factors.

3. The Court below has decided an important question of local law in a way probably in conflict with applicable local decisions in that it has decided that the powers of the trustees could be employed for their own benefit although this holding is directly in conflict with the terms of the trust instruments themselves and with the decisions of the Supreme Court of Michigan which hold that powers of a trustee are powers in trust and must be exercised for the benefit of the trust and that he can take no benefit or advantage of them for himself. *In re Culhane's Estate,* 269 Mich. 68.

4. The decision below has decided another federal question in a way probably in conflict with applicable decisions of this Court in failing to give proper significance

to the fact that the power to change beneficiaries was unexercised thus conflicting with the decision of this Court in the analogous field of the estate tax in *Helvering v. Safe Deposit and Trust Company,* 316 U. S. 56 where this Court held that when a power of appointment was unexercised the property subject thereto was not taxable in the estate of the donee under *Section 302 (a) Revenue Act of 1926* (Section 811 I. R. C.) which is the general gross estate provision corresponding to *Section 22 (a) I. R. C.* for the income tax.

5. The decision of the Circuit Court of Appeals is in conflict with the decision of other Circuit Courts of Appeals on the same matter, *i.e.,* the decision of the 10th Circuit in *Armstrong v. Commissioner,* 143 F (2d) 700 and of the 5th Circuit in *Montgomery v. Thomas,* 146 F (2d) 76. Those Courts held that partnerships must be taxed in accordance with the provisions of *Section 181 et seq. I. R. C.* and that the control factors which exist in partners are the accompaniment of a fiduciary relationship and necessarily incident to all partnerships and must be employed for the purpose of advancing the interest of the business and do not serve to bring into play *Section 22 (a) I. R. C.* The decision of the Court below is directly to the contrary. In the *Armstrong v. Commissioner* case the conflict was even more marked because the partnership was between settlor and his trust exactly as in the case at bar.

6. The Court below has rendered a decision in conflict with the decision of another Circuit Court of Appeals in the same matter in that it is has held that when, as here, the facts are undisputed the ownership of trust property was, rather than a question of local law, a question of fact peculiarly within the competence of the administrative tribunal, the Tax Court, a misapplication of the decision of this Court in *Dobson v. Commissioner,* 320 U. S. 489.

This error was expressly avoided by the 10th Circuit in its decision in *Armstrong v. Commissioner,* 143 F (2d) 700 which held that the question of ownership of trust property was purely one of law which it was the duty of the Circuit Court of Appeals to resolve upon appeal rather than to permit the decision of the Tax Court in such a field of local property law which is outside of its special competency to stand without judicial inquiry or challenge despite its being fraught with error.

7. The Court below has decided a federal question in a way probably in conflict with applicable decisions of this Court in determining that when the facts are undisputed, the ownership of trust property was, rather than a question of local law, a question of fact peculiarly within the competence of the administrative tribunal, the Tax Court, a misapplication of *Dobson v. Commissioner,* 320 U. S. 489. This misapplication of the *Dobson v. Commissioner* case is in conflict with the decision of this court in *Helvering v. Stuart,* 317 U. S. 154 where this court held that the determination of the Circuit Court of Appeals on the question of local law of the nature and ownership of the trust property was to be adopted and preferred, to the decision of the Tax Court on such a subject, thus clearly demonstrating that the jurisdictional limitations of the Dobson case can have no application to this situation.

It is submitted that these are vital questions of tax administration of great importance to taxpayers, the Bar and the administrative officers of the Government and therefore constitutes a question of general and public importance which only this Court can resolve.

Wherefore, Petitioners respectfully pray that a writ of certiorari be issued out of and under the seal of this Court, directed to the United States Circuit Court of Ap-

peals for the Sixth Circuit, to the end that said cause may be reviewed and determined by this Court, as provided by law, and that Petitioners may have such other and further relief or remedy in the premises as to this Court may seem appropriate, and that the judgment of said Circuit Court of Appeals may be reversed by this Honorable Court.

LOUIS HAMBURGER and
SAMUEL HAMBURGER,
Petitioners,

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